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~~No. 97-197~~

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term 1997

LITTON INDUSTRIAL AUTOMATION SYSTEMS, INC., ET AL.,

Petitioner,

v.

NATIONWIDE POWER CORPORATION ET AL,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit.

REPLY BRIEF

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TABLE OF CONTENTS

Page

Argument 1

Important Issues 1

Conflict with Decisions of this Court 2

Conflict Among the Circuits 4

Conflict with the Supreme Court of Florida 5

Conclusion 7

Table of Authorities

Cases

Gauvey v. United States, 291 F.2d 42 (8th Cir. 1961) 4

United States v. McDermott, 507 U.S. 447, 449 (1993) 1, 2, 4

ARGUMENT

Important Issues

Petitioner's assertion that the issues involved in the instant case are important to the administration of the federal tax laws due to the frequency of the fact pattern and the impact of the law on the property rights of creditors of taxpayers was unopposed by Respondent.

The instant case is also critical to the development of the law of tax lien priority. This Court's opinion in *United States v. McDermott*, 507 U.S. 447 (1993) was the most recent in a series of rulings to the effect that *the* law of federal tax lien priority is that an antecedent choate (i.e., "perfected in the federal sense") lien is entitled to priority unless there is a "provision to the contrary." The significance of *McDermott* is that it showed that neither the choateness rule nor equitable principles applied to the tax lien.[1]

The instant case is at least as important as *McDermott* in that it can establish that the FTLA is not a "provision to the contrary" of the common law rule, but rather is merely a relief provision. Since the lower courts have been allowing the IRS to use the FTLA as a weapon against creditors of the taxpayer who would otherwise be entitled to

[1] The private lien in *McDermott* arose from a judgment against the taxpayer which was recorded before the tax lien was recorded. The res was property acquired by the taxpayer after both liens were recorded. This Court held that since the choateness rule meant that the effective date of the judgment lien was delayed until the identity of the res subject to the liens was established, the tax lien was first in time. Even though both liens attached simultaneously, equitable principles were not applied. Hence, the tax lien was superior in full.

priority under the common law rule, the instant case can be a landmark decision in this arena.

Conflict with Decisions of this Court

The conflict between the lower court's opinion and the opinions of this Court is both obvious and material. As stated above, this Court has consistently held that an earlier private lien which is choate (i.e., perfected in the federal sense) is entitled to priority unless there is a "provision to the contrary" (*United States v. McDermott*, 507 U.S. 447, 449 (1993) and cites therein.) In contrast, the opinion of the lower court was that Petitioner's earlier lien was not entitled to priority simply because it failed to meet the definition of a "security interest" provided by the FTLA. The lower court ignored the first in time rule of the federal common law and the concomitant question of whether the FTLA could possibly be interpreted to be a "provision to the contrary."

In effect, the lower court held that the FTLA is *the* law of federal tax lien priority and that the private lien had to meet the definition of a "security interest" under the FTLA in order to be entitled to priority over the tax lien. The result of the lower court's reasoning was that Petitioner lost the lien priority battle even though it would have been entitled to priority if the opinions of this Court had been followed. If that is not a blatantly obvious conflict, then the only way to arrive at a conflict would be outright mutiny.

Respondent uses legerdemain in an effort to disguise the reality that it has no viable argument that there is no conflict between the lower court and this Court. Instead of attempting to rationalize the lower court's ruling with the

opinions of this Court (which is an extraordinarily difficult, if not impossible, task) Respondent took the low route of simply restating Petitioner's positions to be the opposite of what they are and then declaring Petitioner's positions to be "directly refuted" by this Court's opinions.

To see this, consider that Petitioner's common law argument has two main elements. The first is that Petitioner's lien is choate, and thus "perfected in the federal sense." The second is that in an instance where the private lien predates the tax assessment there is no reasonable way to interpret the FTLA as a "provision to the contrary" of the common law rule that the first in time is the first in right.

Respondent restates both of those main elements to be the opposite of what they are. Respondent's argument begins by describing Petitioner's position as though it were that Petitioner's lien is entitled to priority under the first in time rule notwithstanding the *contrary* provisions of the FTLA. (Res. 6) But Petitioner's position is perfectly clear that the FTLA is not a "provision to the contrary" of the first in time rule, that the FTLA is nothing more than a relief provision for persons dealing with the taxpayer, that the FTLA cannot be used as a weapon by the IRS, that the FTLA merely delays the effective date of the tax lien for purposes of the first in time rule, etc.

Restating Petitioner's argument so that it appears to be the opposite of what it really is allowed Respondent to immediately declare that (Res. 6)

> [Petitioner's] contention is directly refuted by this Court's decision in *United States v. City of New Britain*, 347 U.S. 81 (1954).

Of course Petitioner's position would have been directly refuted by the opinions of this Court if Petitioner's position were that the FTLA is a "provision to the contrary" of the first in time rule.

Respondent then goes on to discuss *United States v. McDermott*, 507 U.S. 447, 449 (1993) and concludes that

> The contention of petitioner that a private lien claim that is not "perfected" under this federal standard should "nonetheless" prevail is thus directly refuted by this Court's decisions in *City of New Britain* and *McDermott*. (Res. 7)

Again, Petitioner's position is exactly the opposite of Respondent's characterization. Petitioner claims loud and clear that its lien meets the federal standard. (Did Respondent even read the petition?) And again, Petitioner agrees that its position would be directly refuted by the opinions of this Court if Petitioner's position were that its lien did not meet the federal standard.

Respondent makes Petitioner's case!

Conflict Among the Circuits

Respondent goes on to misconstrue Petitioner's reason for making an argument concerning the Eighth Circuit's decision in *Gauvey v. United States*, 291 F.2d 42 (8th Cir. 1961). Petitioner argued the *Gauvey* case to show that such decision was in conflict with the decision of the lower court — and not, as construed by Respondent, to show that the Eighth Circuit was in conflict with this Court.

Besides that significant mistake, Respondent also misconstrued Petitioner's argument. Petitioner's argument regarding the conflict among the circuits had nothing whatsoever to do with the definition of a "security interest" under the FTLA, as Petitioner's argument was construed by Respondent (Res. 7-8.) Instead, Petitioner's argument was that there was a conflict between the lower court and the Eighth Circuit's *Gauvey* decision because the Eighth Circuit in *Gauvey* held that a private lien which was not recorded (and hence not perfected under state law) was nonetheless entitled to priority over the competing tax lien because it was choate (and thus perfected in the federal sense) before the tax lien arose. That is a direct conflict.

Petitioner pointed out that the Eighth Circuit erred by holding further that the statute provided relief to the private lienholder -- the correct analysis being the statute did not apply at all -- but in any event the Eighth Circuit's reliance on the statute is a clear holding that the precursor to the FTLA was not a "provision to the contrary." The Eighth Circuit specifically refused to read a requirement of perfection under local law into the statute. Since the changes wrought by the FTLA do not change the thrust of the statute, such statutory reliance by the Eighth Circuit is another direct conflict.

Conflict with the Supreme Court of Florida

The final issue addressed in the brief in opposition concerned whether there was a conflict between the decision in the lower court and the Supreme Court of Florida. To begin with, Petitioner reiterates that this issue involves the definition of a "security interest" under the FTLA and that this issue is moot if the FTLA is not a "provision to the

contrary." But more to the point, the conflict between the decision in the lower court and the Supreme Court of Florida is direct and obvious. Not only did the two courts render opposite conclusions about the proper interpretation of the phrase "security interest," but the lower court opined that the earlier case was wrongly decided by the Supreme Court of Florida.

Respondent argues that if the Florida Supreme Court had had the benefit of later Treasury regulations it may have rendered a different opinion. Perhaps, but that argument is rank speculation. The Florida Supreme Court rendered a straight statutory interpretation. In comparison, the lower court struggled mightily to reach a contrary result, ultimately relying upon an arguably misinterpreted regulation which addressed a completely different issue — and in the process opining that Congress erred in rejecting language which the lower court's opinion effectively reinserted into the statute.

Respondent also argued that the lower courts in Florida do not follow the Florida Supreme Court decision. But the only case cited by Respondent in support involves a lien which was perfected under state law through garnishment. Such lien qualified as a "security interest" under any interpretation of the statute, the regulations and the Florida Supreme Court decision.

Respondent's argument that there is no conflict between the decision of the lower court and the Supreme Court of Florida is not persuasive.

CONCLUSION

The issues involved are important to the administration of the federal tax laws and there are material conflicts between the decision of the lower court and the opinions of this Court, the 8th Circuit Court of Appeals and the Florida Supreme Court. The petition for writ of certiorari should be granted.

Respectfully submitted,
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